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FRAUD AND MISREPRESENTATION

SUMMARY

Whilst they are often confused, fraud and misrepresentation are two very different aspects of the law. Most think they are similar, and the laws don't differ for punishment or damages among the two. The key difference that separates fraud from misrepresentation is that fraud is done with an aim of deceiving others whereas that is not the case for misrepresentation. Fraud and misrepresentation are also often confused with the tort of deceit. Another aspect that can be looked at is fraudulent misrepresentation. It arises out of a contract law as a civil tort. There is a rising amount of fraud and misrepresentation not only in India but also around the world. Whether it is credit card fraud or bank fraud, there is a rising problem with very lenient laws. An example right in front of our eyes is the case with Vijay Mallya or Nirav Modi. Both obtained money from the banks by fraudulent ways and then escaped. They need to be brought to justice, the law needs to be amended and there need to be proper penalties for the same.

❖ INTRODUCTION

The word 'fraud' is not defined in the Indian Penal Code. It instead constitutes of doing an action that is fraudulent in nature is. There isn't an independent legislation, yet that deals with fraud as in the United Kingdom or the USA. A person is said to do a thing fraudulently if he does that with the intent to defraud but not otherwise. Thus, in general terms we can say that A deceptive act done intentionally by one party in order to influence another party to enter into a contract is known as fraud and the representation of misstatement, made innocently, which persuades the other party to enter into a contract, is known as misrepresentation.¹

¹ <https://www.prepagent.com/article/the-difference-between-fraud-misrepresentation>

Fraud contains the aspect of intent whereas misrepresentation does not. To prove fraud one must prove mens rea. Imagine yourself as a real estate agent. You tell a potential buyer that the square footage of the house is 2500 whereas you very well know that it is only 1500. This is fraud. Your intention is to sell the house, no matter what. Now, if you tell the potential buyer that it is 2500 when even you believe it is 2500 square feet, it amounts to misrepresentation. Thus, we can say that misrepresentation is a representation of a material fact made by a party who believed it to be true, the other party relied on the statement and entered into a contract based upon the statement, and it later turned out to be false or wrong.

In the first case the contract is completely void but only on the option of the buyer. He can buy the house of 1500 square if he wants to but in the second case the contract is completely null and void.

❖ FRAUD

Fraud is an act which is committed with the intent to cheat and then to obtain some benefit or advantage to which they are not usually entitled to or someone knowingly denies some benefit that is due to which some party is entitled. This can either be wrongful gain or wrongful loss. Whoever does anything with the intention of causing either of these is said to do it 'dishonestly'. Section 420 in the Indian Penal Code deals with Cheating and dishonestly inducing delivery of property. The maximum punishment which can be awarded is imprisonment for a term of 7 year and a fine.² There is a difference between breach of contract and cheating. Breach of contract does not give rise to a criminal prosecution unless intent is proven. The difference between cheating and misrepresentation is that in misrepresentation, which is neither claimed or alleged to be dishonest or fraudulent would not attract the charge of cheating only because the complainant parts with his money on the basis thereof.³

Indian Penal Code recognizes impersonation, counterfeiting, wrong weighing and measurement, misappropriation, criminal breach of trust, cheating, dishonest dealing in property, mischief, forgery, falsification, possessing stolen property and voluntary concealment.

² Indian kanoon

³ "Abdul Fazal Siddiqui vs Fatehchand Hirawat And Another". *Indian Kanoon*. Retrieved 16 May 2017.

The act of committing the crime or fraud can be done in many ways. It can be conducted through the mail, wire, internet and phone. The acts include false insurance claims, tax irregularities, counterfeiting of currency and legal documents, and embezzlement, to false advertising and countless other acts. One of the rising types of fraud is corporate fraud.

In the case of *Therman Ltd vs K.M*⁴ Court highlighted the grounds on which criminal proceedings are to be quashed under Section 482 of the Code and noted the ingredients of Section 420 IPC. The appellant was a non-banking financial institution where the respondents were giving money for dental chairs. The institution where the money was being funded to was, the Rajiv Gandhi Dental College. Not only was money but the required special chairs were going to be given too. The appellant then sued the respondent for not giving the money required and missing chairs. The main offence alleged by the appellant is that the respondents committed the offence under Section 420 IPC and the case of the appellant is that the respondents had cheated him and thereby dishonestly induced him to deliver property.

In the case of *Tholasiram v Duraji*⁵ the court stated that if a buyer purchases products with the intention of never paying from them, then under the contract act, it is counted as an act of fraud. Here, the keyword to be looked at is intention.

In the case of *Pundalikaprabhu v Additional Land Tribunal*⁶ it was stated that if one party makes a representation under a false pretense, it counts as fraud. If this act amounts to an injury they will be punished by the law. An act of fraud is always viewed seriously in the eyes of. A conspiracy to deprive a right of other amounts to fraud and fraud and deception are synonymous in nature. Fraud cannot be saved by the doctrine of *res judicata*.⁷

One of the most famous case if of the 9,000 Crore bank fraud that was committed by Vijay Mallya. Building his rising company which began in 2005, Kingfisher Airlines was grounded in the year 2012. After he landed into crushing debt, it impossible for the struggling airline to continue all of its ongoing operations. The airline currently is also being investigated for

⁴ *Therman Ltd vs K.M*

⁵ *Tholasiram v Duraji*

⁶ *Pundalikaprabhu v Additional Land Tribunal*

⁷ <https://www.casemine.com/search/in/fraud>

suspected diversion of funds and financial irregularities. He borrowed money from many banks to allegedly fund KFA without any proof to pay the creditors back. He was loaned crores of rupees just because of who he was. He then siphoned off the money to buy properties and teams all across the world. He then kept borrowing money from banks and landed in debt. It was only when the law became rigid did, he flee to London.

Let us not forget the Nirav Modi, PNB scam that had taken over the papers just a while back. An 11,400 Crore Rupee fraud was conducted by bankers who used false Letters of Undertakings at PNB's Brady House branch in Fort, Mumbai. The LoUs were opened in favour of branches of Indian banks for import of pearls for a period of one year, for which Reserve Bank of India guidelines lay out a total time period of 90 days from the date of shipment. These guidelines were ignored by overseas branches of Indian banks. They failed to share any documents or verification, which were made available to them by the firms at the time of availing credit from them. The inquiry agency found that Nehal Modi, brother of Nirav Modi had destroyed the devices and had even secured a server located at United Arab Emirates soon after the scam broke out. These dummy firms had been receiving the fraudulent PNB LoUs and were based out in British Virgin Island and other tax sanctuaries.

Looking at the above cases we can see that there are some instances where the judiciary is fair but in the cases of Nirav Modi and Vijay Mallya it has been unfair. The punishment for fraud is fine and a maximum imprisonment of 7 years. This does seem fair when the crime is small but these two have swindled many and because of them, the economy too has taken a toll. The role of various courts has been altered by the adoption of various constitutional norms by the governance of the country.⁸ Various statutory provisions have been made too, to establish the governmental institutions and how they must regulate their conduct. Yes, the government is making strides to lessen the amount of fraud that takes place but there is a lot more that they can work on.

❖ MISREPRESENTATION

⁸ <http://www.legalservicesindia.com/article/1902/role-of-judiciary-in-strengthening-pil.html>

In India, the federal law defines misrepresentation as a "Misconception of Fact". Section 90 of the Indian Penal Code deals with misrepresentation. Consent given firstly under the fear of injury, and secondly under a misconception of fact, is not considered to be consent at all.

It sees that the party who is allegedly accused and has knowledge or reason to believe that the consent was given by the victim in consequence of fear of injury or misconception of fact. Thus, the second part lays importance on the knowledge or reasonable belief of the person who obtains the false consent. It is the Court that has to determine whether the person giving the consent has done so under fear or a misconception of fact. The court should also be satisfied that the person doing the act is conscious of the fact or the consent would not have been given.

Misrepresentation is one of several vitiating factors that can affect the validity of a contract. They include mistake, undue influence and duress.

Misrepresentation applies only to statements of fact, not to opinions or predictions. There are three types of misrepresentations. Innocent misrepresentation is a false statement of material fact by the defendant, who was unaware at the time of contract signing that the statement was untrue. The remedy in this situation is usually rescission of the contract. The second type is a negligent misrepresentation, a statement that the defendant did not attempt to verify was true before executing a contract. This is a violation of the concept of "reasonable care" that a party must undertake before entering an agreement. The remedy for negligent misrepresentation is contract rescission and possibly damages. The third type is fraudulent misrepresentation, statement that the defendant made knowing it was false or that the defendant made recklessly to induce the other party to enter a contract. The injured party will seek to void to contract and recover damages from the defendant.

In contract law, a misrepresentation is a statement made by one contracting party to another which is false, and which encourages the other contracting party to enter into the contract, as a result of which he suffers a loss. These statements often arise in the course of negotiations and do not become part of the contract. Staying silent will not be considered a misrepresentation although there are specific exceptions to this such as misrepresentation by conduct, partly true statements which become a misrepresentation as a result of what has not been said, failure to disclose a change of situation to the other contracting party and where the contract requires the

utmost good faith or constitutes a fiduciary relationship, such as insurance contracts and partnership contracts.⁹

In *Bisset v Wilkinson*, the plaintiff purchased two blocks of land from the defendant for the purpose of sheep farming. During negotiations the defendant said that if the place was worked properly, it would carry 2,000 sheep. The plaintiff bought the place believing that it would carry 2,000 sheep. Both parties were aware that the defendant had not carried on sheep-farming on the land. In an action for misrepresentation, the trial judge said that it was a false statement of fact.¹⁰

In *Smith v Land and House Property Corporation*, the plaintiff put up his hotel for sale stating that it was let to a 'most desirable tenant'. The defendants agreed to buy the hotel. The tenant was bankrupt. As a result, the defendants refused to complete the contract and were sued by the plaintiff for specific performance. The Court of Appeal held that the plaintiff's statement was not mere opinion but was one of fact.¹¹

In *Nottingham Brick and Title Corporation v Butler*, the buyer of land asked the seller's solicitor if there were any restrictive covenants on the land and the solicitor said he did not know of any. He did not say that he had not bothered to read the documents. The court held that even though the statement was literally true it was a misrepresentation. There were restrictive covenants and the contract could be rescinded.¹²

In *Horsfall v Thomas*, the buyer of a gun did not examine it prior to purchase. It was held that the concealment of a defect in the gun did not affect his decision to purchase as, since he was unaware of the misrepresentation, he could not have been induced into the contract by it. His action thus failed.¹³

In *Attwood v Small*, the purchasers of a mine were told exaggerated statements as to its earning capacity by the vendors. The purchasers had these statements checked by their own expert agents, who in error reported them as correct. Six months after the sale was complete the

⁹ <https://www.investopedia.com/terms/m/misrepresentation.asp>

¹⁰ *Bisset v. Wilkinson*

¹¹ *Smith v Land*

¹² *Nottingham Brick and Title Corporation v Butler*

¹³ *Horsfall v Thomas*

plaintiffs found the defendant's statement had been inaccurate and they sought to rescind on the ground of misrepresentation. It was held in the House of Lords that there was no misrepresentation, and that the purchaser did not rely on the representations.¹⁴

❖ FRAUDULENT MISREPRESENTATION

Any entrepreneur understands the basic concept of business that most deals are sealed with a contract, even if it's a handshake. At its core, contract law regulates the transfer of rights from one party to another, holding each party accountable to the agreed-upon terms. It's of utmost importance in any contract that both parties are on the same page and acting in good faith. But if one party makes a false or misleading statement in order to induce another party into a contract, causing some kind of harm, the aggrieved party may sue for fraudulent misrepresentation.

❖ CONCLUSION

The acts done fraudulently are civil wrong and hence the party doing it can be sued in court by the aggrieved party even if the aggrieved party has a means of discovering the truth in the normal course of action. Misrepresentation is not a civil wrong as the party making the wrong representation honestly have no idea about the actual truth and so the aggrieved party cannot sue the other party in court, but it has the option to rescind the contract.¹⁵ Hence, there is an absence of free consent in both the conditions whether it is fraud or misrepresentation that is why the contract is voidable at the option of the party whose consent was so caused.

❖ CASES USED

1. Therman Ltd vs K.M
2. Tholasiram v Duraji
3. Pundalikaprabhu v Additional Land Tribunal
4. Bisset v. Wilkinson
5. Smith v Land

¹⁴ Attwood v Small

¹⁵ www.investopedia.com

6. Nottingham Brick and Tile Corporation v Butler
7. Horsfall v Thomas
8. Attwood v Small

